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STAFF REPORT

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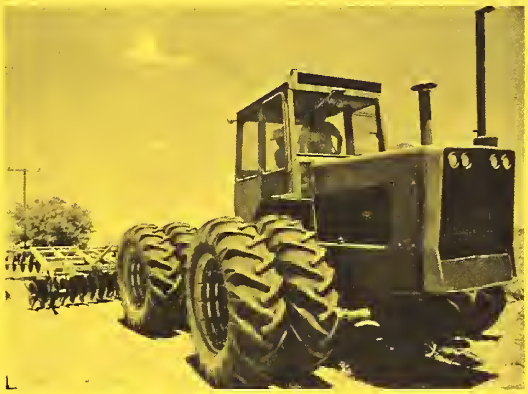

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ABSTRACT

Section 103 of the Food and Agriculture Act of 1977 required the Secretary of Agriculture to report on the effects of prohibiting commodity program payments to corporations and certain other business entities. The results of that study suggest that between 2,700 and 21,000 corporate farm units, tenants of ineligible corporate farms, or partnerships could be affected by such a prohibition. Firms ineligible for payments could not be expected to participate in supply management programs such as set-aside or land diversion. The acreage of wheat, feed grains, cotton, and rice affected by the payment prohibition would range between 425,000 under the most narrowly applied prohibition to approximately 7 million acres if ineligible corporations, tenants of ineligible corporations, and ineligible partnerships were to be denied payments. Little change in agricultural investment by non-farmers could be expected as a result of the prohibition.

Key words: Commodity programs; direct payments; corporations; tenants; partnerships; treasury outlays; participation

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CONTENTS

INTRODUCTION

Section 103 of the Food and Agriculture Act of 1977 requires the Secretary of Agriculture to study the effects of prohibiting commodity program payments to certain corporations and other business entities. This report presents the results of that study. Information is included on the relative importance of the various forms of businesses engaging in farm production and on the impacts on commodity production, price, and program effectiveness of prohibiting payments to these enterprises. The study is limited to a consideration of payments made through the wheat, feed grain, cotton, and rice programs.

The Congress debated whether withholding program payments from certain corporations and partnerships would be an effective way to channel benefits of farm programs to family farms. Their deliberations focused on what groups should be subject to an exclusion if such an approach were adopted. The Senate included a provision in its version of the 1977 Act (S. 275) that would have prohibited payments to certain corporations and partnerships. The House considered but did not include the payment exclusion in its bill; and the provision was deleted in the Conference Committee. Instead, the language of the Food and Agriculture Act of 1977, as ultimately adopted by both Houses of the Congress, mandated that a study be made of the implications of payment prohibitions such as that passed by the Senate on May 27, 1977.1/

Types of Business Entities Analyzed

The record of Congressional deliberations suggests that a major concern of the Congress was with the perceived increase in involvement in farming

1/ The language contained in the 1977 Act and in the Senate version of the Act is shown in the Appendix.

and farm commodity programs by persons who are not primarily engaged in farming. In particular, questions were raised about persons who involve themselves in farming in limited ways through stock ownership, joint ventures, trusts, or other investment mechanisms while providing little day-to-day management of the farm. In view of this legislative history, this study focuses on types of business perceived to have a concentration of investors who are not principally engaged in farming.

Specifically, the study explored the possible effects of prohibiting payments to six types of corporate and partnership farms that would be excluded in the wording of the Senate bill (table 1). Farms that would be able to continue receiving payments under all options considered include sole proprietorships (or husband-wife ownership combinations 2/); political subdivisions and related agencies; and certain tax-exempt organizations including farms operated by churches and other non-profit institutions.

CORPORATIONS AND PARTNERSHIPS IN AGRICULTURE

Corporations and partnerships play an important but not predominant role in farm production. They accounted for 32 percent of total farm sales in 1974, even though comprising only 10 percent of these total number of farms. The average size of a farm partnership was double that of an individually owned farm; the average corporate farm was more than seven times as large. About 90 percent of all partners were related to the other members of the partnership, and only one fourth of the partnerships

2/ Sole proprietorships which are tenants of excluded corporations or partnerships would be excluded from payment under options III, IV and VI.

Table 1.--Alternative groupings of farms to which a payment exclusion could be applied

Option or group	Description
I.	Farms operated by widely-held corporations;1/
II.	Farms operated by widely-held or non-farm corporations;2/
III.	Tenants of widely-held or non-farm corporations;3/
IV.	Combination of groups II and III;
V.	Non-farm partnerships;4/
VI.	Combination of groups IV and V.

1/ "Widely-held" corporations are defined as incorporated businesses with 16 or more shareholders.

2/ "Non-farm" corporations refer to incorporated businesses which are not engaged primarily in farming. Group II, therefore, includes entities encompassed within Group I, as well as farms operated by corporations not primarily engaging in farming.

3/ These refer to tenant-operators of farms owned but not operated by widely-held or non-farm corporations.

4/ These refer to farms operated by partnerships in which either at least one partner or the entire partnership is not primarily engaged in farming.

had more than two partners. Ninety-three percent of the corporations had fewer than 10 shareholders and 79 percent had fewer than five shareholders. The shareholders were related to each other in 87 percent of corporations. Shareholders and partners of most multi-owner farms were actively involved in the management of their businesses. In 1974, fewer than 2,000 corporations had 11 or more shareholders and they were responsible for less than three percent of all farm sales.

Corporations accounted for 18 percent of all farm sales in 1974 with a concentration in the production of fed cattle, turkeys, eggs, fruits and vegetables, and sugar cane (table 2). Grains and cotton accounted for only 10 percent of the farm receipts of corporations whereas grains and cotton accounted for 33 percent of all U.S. farm marketings.

Partnerships accounted for 14 percent of farm receipts in 1974 with their share ranging from 12 to 20 percent for the major commodities. Their commodity mix does not appear to be different from that of sole proprietorships.

DIRECT PAYMENTS IN AGRICULTURE

Direct payments have impacts upon production decisions, and consequently, upon the policy objectives of Government. Their roles and history in policy and production decisions are discussed in this section.

Role in Achieving Policy Objectives

Throughout the history of commodity programs direct payments have been only one of several forms of income support to the farm sector. Supply controls, price supports, export programs, and market development activities are other types of public programs that have been used to increase farm incomes.

Table 2.--Relative importance of commodity group sales for all farm corporations, 1974

Item	Sales by all farm corporations: Share of total marketings of commodity	Sales by all farm corporations: Share of sales by all farm corporation
	- - - Percent - - -	
Grain	4.9	8.2
Cotton	15.8	2.4
Tobacco	3.3	0.4
Other field crops 1/	25.0	10.1
Vegetables	36.9	5.9
Fruits and nuts	31.5	6.3
Nursery and forest products	60.3	7.1
Poultry	28.1	11.9
Dairy	6.3	3.5
Cattle	32.8	40.9
Other livestock	7.7	3.3
All sales	18.2	100.0

1/ Including peanuts, potatoes, sugar beets, sugar cane, popcorn, and mint.

SOURCE: 1974 Census of Agriculture, Vol. IV, Special Reports, Part 5, "Corporations in Agricultural Production."

Direct payments are made to producers both to support and stabilize farm incomes and to induce producers to comply with acreage controls when prospective supplies are expected to exceed demand. Under the current programs, income support is provided by direct payments to farmers with the amount determined by the target-price concept. Target prices, based upon national average costs of production, have been established for each of the six crops (wheat, corn, sorghum, barley, rice, and cotton) considered in this study. If the average market prices for a specified period of the season are less than the target prices, qualifying producers receive deficiency payments to make up the difference. These are guaranteed prices and stabilize producer incomes from year to year from fluctuations due to weather and demand.

To be eligible for these support programs a producer must comply with any set-aside (acreage reduction) requirements in effect. The guaranteed price, therefore, serves as an incentive for complying with acreage-reduction requirements. If a producer elects not to set-aside acreage, he is ineligible for program payments and must accept the market price for his commodities.

A second feature of the current program, similar to deficiency payments, is the disaster payments program. Eligible producers, prevented from planting or suffering low yields can receive payment for the program commodities. To be eligible, the producer must also comply with set-aside requirements. This program is, in essence, free insurance--it removes fluctuations in income due to natural hazards.

In addition, direct payments are made on a contractual basis to producers who divert cropland to conserving uses. These diversion payments would also be subject to a payment prohibition.

Payments in an Historical Context

Direct payments were first made to farmers in the 1930's as part of the comprehensive Government programs to improve depressed conditions throughout agriculture. Payments were first made to wheat and cotton producers in 1933 and to corn producers in 1934. Payments were used intermittently during the 1940's and 1950's. Beginning in 1960, payments have played a more prominent role than in earlier years.

Prior to 1970 some operators received in excess of a million dollars in annual commodity program payments. Legislation passed in 1970 imposed an upper limit of $55 thousand on payments for each of the wheat, feed grain, and cotton programs in which an operator might participate. This payment ceiling was implemented as an attempt to restrict the payment level to that which a moderate to large size family farm would receive. The payment limit was reduced to a combined total of $20 thousand for all programs in 1974 and was subsequently raised in 1978 to $40 thousand for wheat, feed grains, and cotton. The 1977 Act specified that the limit for the crops, including rice, would be raised to $50 thousand beginning in 1980.3/ Disaster payments were exempted from the limitation.

The level of direct payments to participants in commodity programs has varied considerably over recent years. They reached a high of $4.0 billion in 1972, but dropped to $0.5 billion two years later (see table 3). Direct

3/ The payment limitations have prevented the extremely large farms from receiving large payments, although many were able to circumvent the limitation through leasing and other arrangements.

Table 3.--Direct government payments in comparison to selected farm sector financial indicators, 1969-77

Item	1969	1970	1971	1972	1973	1974	1975	1976	1977
	Calendar Year								
	- - Million dollars - - -								
Direct government payments	3,794	3,717	3,145	3,961	2,607	531	807	734	1,819
Net income from farming after inventory adjustments	14,293	14,151	14,633	18,665	33,349	26,130	24,475	18,750	20,543
Farm marketings	48,179	50,539	52,859	61,190	87,063	92,449	88,209	94,501	96,084
Production expenses 1/	42,115	44,424	47,367	52,315	65,562	72,210	75,863	82,972	87,969
Value of crop production	24,038	28,898	26,844	34,253	54,817	56,399	56,778	55,655	56,634
Value of livestock production	23,083	25,089	25,039	29,410	38,316	35,067	34,930	37,712	38,249
Capital Gains 2/: Total farm assets	12,376	11,199	23,131	40,425	79,475	37,391	58,377	76,777	50,011
Real estate	8,252	9,118	18,111	29,468	62,808	42,313	50,467	68,998	43,621

1/ Includes Government payment to non-operator landords.

2/ Capital gains on physical farm assets include appreciation in real estate assets plus increases in value of non-real estate capital goods and inventories.

SOURCES: Various issues of Farm Income Statistics, Crop Values, Balance Sheet of the Farm Sector, and Agricultural Statistics, published by U.S. Department of Agriculture.

payments were consistently high from 1961 to 1973 when farmers received an average of $2.8 billion per year. Most payments have been made to producers of five major crops: wheat, cotton, corn, barley, and sorghum. Rice payments were started in 1976 following passage of the Rice Production Act of 1975. Payments were highest relative to crop values under the wheat and cotton programs (table 4). In 1967, cotton program payments equaled the market value of the crop, and payments were nearly half the value of the wheat crop in 1969 and 1970. Producers received an average of $2.2 billion per year through programs for the six crops during the years 1965 to 1977. For all six crops payments equaled 13 percent of the value of production over the 13-year period, even though payments were less important during 1974-76 when market prices for grains were favorable.

The amount of payments received by farmers has been small compared to receipts from farm marketings (table 3). However, the payments have been much more important relative to net farm income, averaging 12 percent of the net during 1969-77, exceeding 25 percent in the late 1960's.

Compared to total returns to farmers (income plus asset appreciation), direct payments are not large. Capital gains, most of which have been in farm real estate, have averaged more than 2-1/2 times the amount of farm income since 1971 and have exceeded income from farming in every year during the years 1971 to 1977 (table 3). Government payments were only 5 percent as much as asset appreciation during this period. Therefore, for nonfarm or corporate investor, substantial returns would be possible through long-term capital gains, even without eligibility to receive direct payments.

There are substantial differences among regions and types of farms but these factors are general throughout the farm sector.

Table 4 --Value of production and Government payments for crops, 1965-77.

Year	Wheat: Value of production	Wheat: Government payments	Wheat: Payment as pct. of value of production	Corn for grain: Value of production	Corn for grain: Government payments	Corn for grain: Payment as pct. of value of production	Barley: Value of production	Barley: Government payments	Barley: Payment as pct. of value of production
	million dollars		percent	million dollars		percent	million dollars		percent
1965	1774.5	509.2	28.7	4754.2	1094.1	23.0	399.6	62.6	15.7
1966	2129.9	681.3	32.0	5171.0	1028.0	19.9	411.8	47.3	11.5
1967	2090.1	727.1	34.8	5044.2	730.6	14.5	374.4	-	-
1968	1929.1	746.0	38.7	4825.6	1165.6	24.2	390.2	-	-
1969	1795.7	855.9	47.7	5416.0	1365.3	25.2	377.9	46.0	12.2
1970	1803.2	871.0	48.3	5514.4	1225.1	22.3	400.4	44.7	11.2
1971	2165.7	885.7	40.9	6095.0	893.1	14.7	453.7	-	-
1972	2704.1	858.7	31.3	8732.7	1458.9	16.3	507.2	107.2	21.1
1973	6719.2	478.2	7.1	14401.8	[illegible]	6.3	888.7	77.7	8.7
1974	7338.4	-	-	14121.8	244.2	1.7	833.8	16.0	1.9
1975	7534.9	-	-	14769.4	89.9	.6	894.7	4.9	.5
1976	5851.4	-	-	13471.8	181.0	1.3	829.7	9.5	1.1
1977	4677.3	1174.2	25.1	12933.0	281.1	2.2	749.0	121.5	16.2
1965-77 av.	3731.9	599.0	16.0	8867.0	821.5	9.3	578.2	41.3	7.1

Year	Sorghum for grain: Value of production	Sorghum for grain: Government payments	Sorghum for grain: Payment as pct. of value of production	Upland cotton: Value of production	Upland cotton: Government payments	Upland cotton: Payment as pct. of value of production	Rice 1/: Value of production	Rice 1/: Government payments	Rice 1/: Payment as pct. of value of production
1965	659.1	225.0	34.1	2086	69.3	3.3	376.2	-	-
1966	729.6	219.9	30.1	981	774.0	78.9	421.0	-	-
1967	744.2	136.4	18.3	938	935.0	99.7	444.0	-	-
1968	690.6	203.1	29.4	1197	783.5	65.5	520.5	-	-
1969	771.5	232.2	30.1	1040	823.2	79.2	447.2	-	-
1970	780.1	236.9	30.4	1110	914.9	82.4	433.2	-	-
1971	904.7	167.0	18.5	1399	819.4	58.6	458.2	-	-
1972	1107.7	289.3	26.1	1778	808.3	45.5	574.0	-	-
1973	1995.2	183.4	9.2	2747	713.5	26.0	1280.0	-	-
1974	1742.5	68.2	3.9	2346	127.8	5.4	1261.4	-	-
1975	1775.0	19.7	1.1	2023	117.6	5.8	1067.7	-	-
1976	1450.1	34.5	2.4	3223	98.0	3.0	811.5	128.8	16.3
1977	1368.0	167.9	12,3	3521	58.3	1.8	928.5	3.9	.4
1965-77 av.	1132.2	167.9	14.8	1876.1	542.6	28.9	694.2	66.4	9.6

Year	Six crop total: Value of production	Six crop total: Government payments	Six crop total: Payment as pct. of value of production
1965	10049.6	1960.2	19.5
1966	9844.3	2750.0	27.9
1967	9635.0	[illegible]	26.2
1968	9553.0	2898.4	30.3
1969	9848.3	3322.6	33.7
1970	10041.3	3295.6	32.8
1971	11482.3	2765.2	24.1
1972	15404.6	3532.9	22.9
1973	28031.9	2362.5	8.4
1974	27644.0	456.2	1.7
1975	28094.7	232.1	.8
1976	25637.5	451.3	1.8
1977	24176.6	1817.4	7.5
1965-77 av.	16879.5	2130.6	12.9

1/ Direct payments for rice were initiated with the 1976 crop as a result of the Rice Production Act of 1975. The averages for rice payments are based on 1976 and 1977.

Source: 1978 ASCS Fact Sheets.

Payment Prohibitions and Production Decisions

If commodity programs are changed to prohibit payments to certain producers, those affected will not likely participate in Government programs and, accordingly, may adjust their mix of crops. Adjustments would be expected at least in the years when supply controls are in effect, since there would be minimal benefits from continuing to participate. The following discussion of the wheat program and economic conditions for 1978 illustrates this point.

The 1978 wheat program provided a price support (the loan rate) of $2.35 per bushel, and an income support (target price) level of $3.40 for producers who set aside two acres of land for every ten that they planted to wheat. Complying producers were also eligible for the disaster payments program. The market price for wheat averaged $2.88 during the first five months of the marketing year; hence, the complying producers received a deficiency payment of $.52 per bushel. The payment is the product of the wheat acreage planted for harvest _times_ the normal crop yield of the farm _times_ the deficiency payment per bushel.

If the producer were ineligible for disaster and deficiency, or diversion payments, the only direct benefits for which a participant would be eligible would be price support loans and storage payments for grain held in the farmer-owned reserve. However, the market price for wheat would remain near or above the loan support level unless a large proportion of producers did not participate in the program. As a result, the producer could expect to receive at least the loan price without complying with any production controls. Most producers are unable to make major shifts away from program crops because of specialization of their farms and

adaptation of their areas to certain crops. Consequently, there is little reason to anticipate major shifts among crops as a result of a payment prohibition.

In essence, as long as the market price remains higher than out-of-pocket costs per bushel, any producer who cannot receive payments would maximize his profits by putting into production his full acreage, consistent with rotational and fallowing requirements. Therefore, the level of production for the affected program crops would likely increase as a result of a payment prohibition.

IMPACTS OF A PAYMENT PROHIBITION

This section considers the impact on commodity production and market price of a payment prohibition applied to the groups outlined in table 1.

Methods

The analysis of corporations is based on data assembled for this study by the Agricultural Stabilization and Conservation Services (ASCS). Data for the partnership analysis come from the 1974 Census of Agriculture and a follow-up survey of partnerships in 1976.

For this analysis, ASCS county offices provided information on each farm owned, operated, or owned and operated by an incorporated business, including those in which an incorporated business had only partial ownership.4/ Data were supplied for 64,080 ASCS farm units with which a corporation was involved. These farms were associated with about 42

4/ Hereafter, farms identified and reported by the ASCS county offices for this study are referred to as "incorporated farms."

thousand incorporated businesses.5/ Since ASCS data on production and programs for wheat, feed grains, cotton, and rice pertain to farms rather than corporations, the analysis that follows is related to farms on record with ASCS for which there is corporate involvement, and not to the number of corporations that would be excluded from payments.

The data for partnerships were considerably less extensive than that for corporations. Information from the 1974 Census of Agriculture and the 1976 Survey of Farm Partnerships is summarized in Table 5. In this analysis, it is assumed that firms excluded from payments would be those reporting one or more partners receiving his primary income from other sources (table 5). In some partnerships the "other source of income" is another farm; this would result in the partnership being incorrectly listed in the excluded category. In addition, partnership businesses for which the primary business activity is not farming are not tabulated; this results in undercounting of partnerships engaged in farming. The magnitude of these errors cannot be estimated but they are, at least, partially offsetting.

The partnerships which would be excluded from payment are estimated to be 18,752 grain producers and 1,638 cotton producers, with sales of $731 million and $107 million, respectively. They represent about one-third of all partnerships producing grain or cotton. Their sales were approximately 3 percent of all grain and 4.7 percent of the cotton marketed. The grain production shown above includes other grains (such as soybeans) for which neither a program nor an exclusion applies. However, assuming

5/ The difference in number of incorporated farms and corporations is due to some corporations having more than one "farm" as defined by ASCS.

Table 5.--Partnerships in U.S. farm production, extent of nonfarm activities, and impacts of a prohibition of Government payments

Item	Unit	2	3	4	5	6 or more	Total
		Number of partners					
		- - - All parnterships - - -					
Partnerships producing any farm commodity	No.	61,775	13,423	4,964	742	834	81,738
Percentage that have a partner with primary income from sources outside the partnership	Percent	34.2	40.9	52.1	64.3	77.3	37.1
Partnerships reporting grain sales	No.	39,235	8,216	2,535	393	517	50,896
Grain sales by partnerships	Mil.dol.	1,413	353	135	19	29	1,949
Partnerships reporting cotton sales	No.	3,338	561	374	39	61	4,373
Cotton sales by partnerships	Mil.dol.	159	56	34	4	13	265
		- - - Partnerships excluded from payments 1/ - - -					
Grain producers	No.	13,418	3,360	1,321	253	400	18,752
Sales of grains	Mil.dol.	483	144	70	12	22	731
Cotton producers	No.	1,142	229	195	25	47	1,638
Sales of cotton	Mil.dol.	54	23	18	2	10	107

1/ Based on the percentage of partnerships that have one or more partners with primary source of income from other sources (second-line).

SOURCE: Survey of Farm Partnerships by Bureau of Census and ESCS estimates.

they produce the same mix of crops as other farms, the excluded partnerships would have produced about 1.7 million acres of wheat, 3.0 million acres of corn, barley, and sorghum; and 580 thousand acres of cotton in 1978.

The estimates of the potential change in production for both corporations and partnerhips are based on several assumptions. First, it was assumed that farms excluded from commodity program payments would continue to remain in production since out-of-pocket costs would be below expected market prices. Second, it was assumed that these producers would undertake few major shifts in crop production but would merely return their set-aside and diversion acreage to production. Third, it is expected that the excluded participants would not return to production all of the land that qualifies as set-aside or diversion under production adjustment programs due to the "slippage" effect of marginal lands. Based upon these assumptions and previous research, it is expected that about 60 percent of wheat set-aside and 80 percent of feed grain and cotton set-aside or diversion acres would be returned to production. It is assumed that these acres would only be 90 percent as productive as the average land for the farm.

Specific legislative provisions would determine which groups among the 6 options (table 1) would actually be excluded from participation in government payments.

Results

The impacts of applying payments prohibitions to each of the six groups are presented in this section. Numbers of units affected, total acreages and production, as well as program participation in 1978 are presented for each option.

Option I. Farms Operated by Widely-Held Corporations

The provision included in the Senate version of the 1977 Act (S. 275) would have prohibited payments to corporations with one exception--those qualifying as small business corporations (Subchapter S corporations) as defined by the Internal Revenue Service. These would remain eligible regardless of the primary business activity of the corporation or its stockholders. One of the criteria to qualify as a small business corporation is that there be no more than 15 shareholders. The excluded corporations are termed widely-held corporations. As in the Senate bill, tenants of ineligible corporations could continue to receive payments.

From the ASCS data, it was determined that about 2,700 incorporated farms would be ineligible to receive payments (table 6).6/ However, in 1978 only about 1,400 of these farms produced any of the six crops to which an exclusion would apply. Their output of the six crops totaled 425 thousand acres. Approximately 300 of these farms produced 96 thousand acres of wheat. Feed grains were produced on 900 farms with a total of 210 thousand acres of corn, sorghum, and barley. Fewer than 150 farms produced 54 thousand acres of cotton. The exclusion would have applied to 67 rice farms that produced 63 thousand acres of rice. Only 700 of the farms that would be excluded were participants in the 1978 program. The participants produced less than 300 thousand acres of the six program crops.

6/ The 2,700 ineligible farms total 8 percent of those for which a determination could be made. There are about 8,300 for which the eligibility could not be determined due to lack of information at the ASCS county office. If the same percentage of these would be excluded as for the known group, this analysis undercounts by about 600 farms. The major conclusions would remain unchanged.

TABLE 6.--OPTION I--Incorporated farms operated by corporations having 16 or more shareholders

Crop	Producers		Participants in support program			Potential production and price changes after exclusion 2/		
						Acreage	Production	Corresponding price changes
	Number	1,000 acres	Number	1,000 Acres	Percent 1/	1,000 Acres	1,000 bu. 3/	Dollar per bushel
Wheat	321	96	207	60	62.7	+7.2	+206	4/
Feed grains	961	204	354	127	62.2	---	---	4/
Corn	693	129	---	72	56.0	+10.3	+938	4/
Sorghum	118	25	---	16	64.9	+1.7	+88	4/
Barley	105	50	---	38	76.7	+3.5	+156	4/
Cotton	136	54	99	23	42.2	+0.3	+127	4/
Rice	67	63	54	54	86.3	---	---	4/

1/ As a percentage of producers acreage.

2/ These estimates were based on the set-aside and diverted acreage that could be returned to production by excluded participants. The estimates also reflect a slippage of acreage of 40 percent for wheat, 20 percent for feed grains and cotton. Crop yields employed to calculate production changes were that of the 1978 national harvested yield per acre for individual crops.

3/ Except for cotton which is in thousands of pounds.

4/ Less than 0.5 cents per pound or bushel.

SOURCE: Agricultural Stabilization and Conservation Service.

Excluding these producers would result in the following production adjustments. An additional 22 thousand acres of the six crops affected would be planted as a result of a payment prohibition to corporations with 16 or more shareholders. Wheat production would increase 200 thousand bushels from 7 thousand additional acres. Fifteen thousand acres of feed grains would be returned to production by the excluded producers. More than 10 thousand acres would be in corn. Estimated changes in commodity prices corresponding to these production changes would be less than one-half cent per bushel of grain or pound of cotton.

Option II. Farms Operated by Widely-Held or Nonfarm Corporations

This group includes farms operated by widely-held corporations as discussed above, plus farms operated by corporations not engaged primarily in farming regardless of the number of shareholders. More than 8,200 incorporated farms would be ineligible for payments under this exclusion (table 7).7/ In 1978 about 3,200 of these farms produced one or more of the program crops. The total wheat acreage of the six program crops was 700 thousand acres. Wheat was grown on 700 of these farm units (165 thousand acres). Feed grains were produced on more than 2,200 farms for a total of 390 thousand acres of corn, sorghum, and barley. Fewer than 250

7/ This number is about 20 percent of the farms for which a determination of eligibility could be made. Since the ASCS County office did not always know whether a corporation is primarily engaged in farming or if there are 16 or more stockholders, eligibility could not be determined for over 3,000 farms. If the same percentage of these farms were ineligible as for those where a determination could be made, the number is undercounted by about 2,000 farms. This level of underenumeration would not affect the major conclusions.

TABLE 7.--OPTION II--Incorporated farms operated by corporations having 16 or more shareholders or engaging primarily in nonfarm business

Crop	Producers		Participants in support program			Potential production and price changes after exclusion 2/		
						Acreage	Production	Corresponding price changes
	Number	1,000 acres	Number	1,000 Acres	Percent 1/	1,000 Acres	1,000 bu.3/	Dollar per bu.
Wheat	714	165	418	102	62.0	+12.2	+349	4/
Feed grains	2,227	391	893	216	55.3	---	---	4/
Corn	1,759	285	---	139	49.1	+20.6	+1,879	4/
Sorghum	250	44	---	30	68.9	+3.4	+169	4/
Barley	218	62	---	46	74.0	+4.3	+191	4/
Cotton	243	74	173	34	45.7	+0.6	+232	4/
Rice	90	73	77	64	88.0	---	---	4/

1/ As percentage of producer acreage.
2/ These estimates were based on the set-aside and diverted acreage that could be returned to production by excluded participants. The estimates also reflect a slippage of acreage of 40 percent for wheat, 20 percent for feed grains and cotton. Crop yields employed to calculate production changes were that of the 1978 national harvested yield per acre for individual crops.
3/ Except for cotton which is in thousands of pounds.
4/ Less than 0.5 cents per pound or bushel.
SOURCE: Agricultural Stabilization and Conservation Service.

of the excluded farms produced 74 thousand acres of cotton. Rice was grown on 90 of the excluded farms (73 thousand acres).

About 1,600 of the farms that would be excluded under this definition participated in a 1978 program. They grew approximately 400 thousand acres of the six crops.

As shown in table 7, excluding widely-held or nonfarm corporations would result in increased production of the six crops by approximately 40 thousand acres. Wheat production would increase by 12 thousand acres, feed grains by 28 thousand acres, and cotton by about 600 acres The increased production would be 350 thousand bushels of wheat, 2 million bushels of feed grains and 230 thousand pounds of cotton. Prices for the crops would decline by less than one-half cent per bushel (per pound of cotton) as a result of this increase in production.

Option III. Tenants of Widely-Held or Nonfarm Corporations

The Congress directed that a payment prohibition be considered separately for tenants because there is a likelihood that ineligible corporations would be able to circumvent the exclusion by leasing the land to an eligible farmer. A payment exclusion for tenants of ineligible corporations would affect in excess of 9,200 farms, a number slightly greater than if the exclusion were to apply only to operators.8/ About 6,500 of these farms produced one or more of the six crops for a total of 900 thousand acres (see table 8). Approximately 190 thousand acres of wheat

8/ The number is about 60 percent-of the farms for which a determination of eligibility could be made. There are in excess of 4,000 farms for which a determination could not be made. If the above percentage applies, the count would be underestimated by about 2,600 farms which, even though a substantial number, would not significantly change the major conclusions.

Table 8.--OPTION III--Tenants of corporations having 16 or more shareholders or engaging primarily in nonfarms business

Crop	Producers		Participants in support program			Potential production and price changes after exclusion 2/		
						Acreage	Production	Corresponding price changes
	Number	1,000 acres	Number	1,000 acres	Percent 1/	1,000 acres	1,000 bu. 3/	Dollar per bushel
Wheat	1,595	191	941	123	64.5	+14.7	+419	4/
Feed grains	4,216	500	1,753	202	40.4	---	---	4/
Corn	3,339	378	---	135	35.6	+19.8	+1,811	4/
Sorghum	571	50	---	38	75.3	+ 4.0	+200	4/
Barley	306	71	---	30	41.7	+ 2.6	+117	4/
Cotton	512	170	325	83	48.9	+ 1.6	+612	4/
Rice	117	45	103	34	75.6	---	---	4/

1/ As a percentage of producers acreage.
2/ These estimates were based on the set-aside and diverted acreage that could be returned to production by excluded participants. The estimates also reflect a slippage of acreage of 40 percent for wheat, 20 percent for feed grains and cotton. Crop yields employed to calculate production changes were that of the 1978 national harvested yield per acre for individual crops.
3/ Except for cotton which is in thousands of pounds.
4/ Less than 0.5 cents per pound or bushel.
SOURCE: Agricultural Stabilization and Conservation Service.

were grown on 1,600 of these farms. Feed grains were produced on 4,200 farms (500 thousand acres). Only 500 farms, which produced 170 thousand acres of cotton would be excluded from payments as tenants of ineligible corporations.

As a result of this exclusion production of the six crops would increase by approximately 43 thousand acres. This impact is slightly greater than in the previous two cases. The impact on commodity prices would be negligible.

Option IV. Excluded Corporations and Their Tenants

This alternative would exclude farms operated by widely-held or nonfarm corporations as well as tenants of such corporations. It is a combination of Option II and III. If these entities were excluded from payments, more than 17 thousand farm units would be affected (table 9). About 10 thousand of these farms produced one of the six program crops in 1978 for a total of 1.6 million acres. About 6,500 of these farms grew feed grains on 900 thousand acres. Cotton was produced on 750 farms; rice on approximately 200 farms. These farms accounted for 240 thousand acres of cotton and 120 thousand acres of rice.

If the 17 thousand farm units associated with ineligible corporations and tenants were excluded from program payments, the amount of land returned to production would include 27 thousand acres of wheat, 54 thousand acres of feed grain, and 2 thousand acres of cotton. This would result in increased production of 770 thousand bushels of wheat, 4.4 million bushels of feed grains, and a negligible amount of cotton. The corresponding market price decrease for wheat would be less than one cent while the decrease in feed grain and cotton prices would be less than one-half cent.

TABLE 9.--OPTION IV-- Incorporated farms operated by or leased from corporations having 16 or more shareholders or engaging primarily in nonfarm business

Crop	Producers		Participants in support program			Potential production and price changes after exclusion 2/		
						Acreage	Production	Corresponding price changes
	Number	1,000 acres 2/	Number	1,000 acres	Percent 1/	1,000 acres	1,000 bu. 3/	Dollar per bushel
Wheat	2,309	356	1,359	225	63.2	+26.9	+768	4/
Feed grains	6,443	891	2,646	418	46.9	---	---	4/
Corn	5,098	663	---	274	41.3	+40.4	+3,690	4/
Sorghum	821	94	---	68	72.3	+7.4	+369	4/
Barley	524	133	---	76	57.1	+6.9	+308	4/
Cotton	755	244	498	117	48.0	+2.2	844	4/
Rice	207	118	180	98	83.0	---	---	---

1/ As percentage of producer acreage.
2/ These estimates were based on the set-aside and diverted acreage that could be returned to production by excluded participants. The estimates also reflect a slippage of 40 percent for wheat, 20 percent for feed grains and cotton. Crop yields employed to calculate production changes were that of the 1978 national harvested yield per acre for individual crops.
3/ Except for cotton which is in thousands of pounds.
4/ Less than one cent per bushel for wheat and .5 cents per bushel or pound for other commodities.
SOURCE: Agricultural Stabilization and Conservation Service.

Option V: Excluded Partnerships

It is assumed that a payment exclusion applied to partnerships would encompass any business in which one or more partners' primary source of income was from nonfarm sources, or one in which the business itself was not primarily engaged in farming. An alternative which is probably more consistent with the Senate language (S. 275), would be to apply the partnership exclusion more narrowly to partnerships in which a nonfarm corporation is one of the partners. However, there were only 13 limited partnerships of this type in grain production in 1976, and they marketed a negligible share of the total sales. None was engaged in cotton production in 1976. This limited partnership exclusion can, therefore, be dismissed as being without impact at this time.

There are no data available on participation of partnerships in commodity programs but there is no reason to believe that their participation rate is different from that of sole proprietorships.

A payment prohibition, if applied to partnerships, would result in a production increase for the six payment crops of approximately 390 thousand acres, based upon 1978 conditions (table 10). Grain production (wheat and feed grain) would increase by 20 million bushels. Cotton production would increase by about 5 million pounds, or 12,000 bales. This production increase would result in a price decrease of about 2 cents per bushel for wheat and 1 cent per bushel for the three feed grains; the impact on cotton prices would be negligible.

TABLE 10.--OPTION V--Partnerships having one or more nonfarm partners

Crop	Producers 1/		Participants in support program			Potential production and price changes after exclusion		
						Acreage	Production	Corresponding price changes
	Number	1,000 acres	Number	1,000 acres	Percent 2/	1,000 acres	1,000 bu. 3/	Dollar per bushel
Wheat	---	1,982	---	1,406	71	+169	+4,800	-.02
Corn	---	2,392	---	978	41	+145	+13,210	-.01
Sorghum	---	494	---	365	74	+39	+1,934	-.01
Barley	---	300	---	193	64	+21	+916	-.01
Cotton	---	628	---	530	84	+14	+5,304 3/	---4/

1/ The number of producers and participants was not available. To determine acreages planted by partnerships for individual crops, the total national acreage planted to each crop in 1978 was multiplied by .03, the estimated share of grain sales by partnerships, for cotton, 0.047. Acreage estimated to be in compliance with each program was then calculated by multiplying the national compliance percentage for each crop by the estimated planted acreage of partnerships. Potential acreages of crops to be returned to production were then determined by the set-aside and diversion percentages for wheat, feed grain and cotton. The estimated creages were adjusted to allow for slippage for wheat at 40 percent, and feed grain and cotton, 20 percent.
2/ As percentage of producer acreage.
3/ 1,000 pounds of cotton.
4/ The estimated change in cotton prices was not significant.

Option VI: Excluded Corporations, Their Tenants, and Partnerships

This is the broadest category of exclusion--farms operated by all widely-held or nonfarm corporations, tenants of such corporations, and ineligible partnerships. It is a combination of options IV and V, as shown in table 1. If this group of farms were excluded from program payments, about 21 thousand partnerships and more than 17 thousand farm operated by corporations or their tenants would be affected (table 11). It is estimated that these farms collectively planted some 2 million acres of wheat, 4 million acres of feed grains, and nearly 900 thousand acres of cotton. About 70 percent of the wheat acreage and 50 percent of the acreage of feed grains were committed to the 1978 programs.

The prohibition of program payments to this group of farms would result in 200 thousand acres of wheat, 260 thousand acres of feed grains, and 15 thousand acres of cotton returning to production. Both wheat and feed grain prices would decline slightly, with wheat prices dropping about 3 cents per bushel; and prices of corn, sorghum, and barley each falling by about 2 cents per bushel. The impact on cotton prices would be negligible since this acreage was only one tenth of one percent of the 1978 total.

CHANGE IN COMMODITY PROGRAM PAYMENTS

Government expenditures would be affected in two ways by a payment prohibition: excluded producers would no longer receive payments, while others could receive higher deficiency payments resulting from decreases in market prices. Excluding some farm business entities would obviously reduce Treasury outlays for deficiency, diversion, and disaster payments to these former program participants. There would be increases in deficiency payments to remaining partic[illegible] if the increased levels of

TABLE 11.--OPTION VI--Excluded corporations, their tenants, and partnerships

Crop	Producers		Participants in support program			Potential production and price changes after exclusion 4/		
						Acreage	Production	Corresponding price changes
	Number 1/	1,000 acres 2/	Number	1,000 acres	Percent 3/	1,000 acres	1,000 bu.5/	Dollar per bushel
Wheat	---	2,338	---	1,631	70	195.9	5,568	-.03
Corn	---	3,055	---	1,252	41	185.4	16,900	-.02
Sorghum	---	588	---	433	74	46.4	2,303	-.02
Barley	---	433	---	269	62	27.9	1,224	-.02
Cotton	---	872	---	647	74	16.2	6,148	--- 6/

1/ See footnote 1 to Table 10.
2/ See footnote 2 to Table 9 and footnote 1 to table 10.
3/ As percentage of producer acreage.
4/ These estimates were based on the set-aside and diverted acreage that could be returned to production by excluded participants. The estimates also reflect a slippage of acreage of 40 percent for wheat, 20 percent for feed grains and cotton. Crop yields employed to calculate production changes were that of the 1978 national harvested yield per acre for individual crops.
5/ Except for cotton which is in thousands of pounds.
6/ The estimated change in cotton price was not significant.

production by farms excluded from participation in the programs lower farm prices. The result could be a net increase in total Government program costs as this analysis projects.

The estimates of changes in production and price levels shown in table 6 through 11 were employed to project the magnitude of change in commodity program payments for two of the previously defined groupings. These two options (IV and VI) indicate the widest range of change in program payments that could be expected. Treasury outlays for commodity loans are ignored, since an outlay in one time period is generally offset by a receipt in a later period.9/

If the payment prohibition is applied as in Option IV (both ineligible corporations operating farms and their tenants), the net change in expenditure is an estimated $9 million decrease (table 12). Based upon 1978 conditions, it is estimated that the prohibition would result in the elimination of $15 million in payments to ineligible entities. However, the increased production attributable to the prohibition would result in approximately a one-half cent decrease in the price of wheat. The decline in the price of wheat could result in increased deficiency payments to program participants.10/ Assuming that 42 million acres, or 1.3 billion bushels, of wheat were subject to the program and that the payment rate per bushel increased by one-half cent, the remaining participants would receive an additional $6.5 million in deficiency payments under the wheat program. Thus, the net savings to the Government would be about $9 million.

9/ It may be noted, however, that loan outlays normally increase when market prices decrease, so that the Government could have larger outlays in the short run.

10/ The payment rate is rounded to the nearest cent so that the actual increase would be either zero or 1 cent depending upon the exact change in price.

If the payment exclusion is applied as in Option VI (ineligible partnerships and corporations and their tenants) the effects would be to increase Government costs by about $27 million based upon 1978 conditions. Ineligible partnerships, being a much larger group than excluded corporations, would return a substantial amount of set-aside and diversion acreages to production. The larger supply would cause prices to decrease enough that deficiency payments to remaining participants would rise by about $114 million. This increase in deficiency payments would more than offset the $87 million savings from the payment exclusion; thus, the result would be a $27 million net increase in Government outlays.

CONCLUSIONS

This analysis indicates that large-scale or nonfarm corporations play a significant, but by no means predominant, role in the production of commodities for which there are Government programs. There is little evidence that payments made through commodity programs provide the primary incentive for corporations and partnerships to enter agricultural production. A large share of corporations, particularly those with non-farmer investors, produce commodities for which there are no direct payments, such as fruits and vegetables, fed cattle, and poultry. Processors for these commodities have perceived advantages in integrating backward into production of commodities.

Partnerships produce approximately the same mix of commodities as sole proprietorships; however, partnership farms are about twice the size of those of sole proprietorships. Most partnerships are between small numbers of related individuals.

Direct payment programs have not given impetus for a surge in investment by those not primarily engaged in farming. Land appreciation and capital gains taxation appear to be stronger influences. A large percentage of farmland continues to be purchased by farmers who wish to expand the size of their operations. Even if nonfarmers are excluded from receiving Government program payments, it is doubtful that such a measure would greatly affect who invests in American agriculture. A prohibition of this nature would only marginally discourage the purchase of farms by business entities ineligible to receive payments. With potential earnings through land appreciation being about 20 times larger than direct payments by government, many excluded business entities would continue to invest in agriculture as long as out of pocket costs can be covered. Those businesses for whom capital gains is a principal objective woul probably not shift their investments, particularly if land appreciation were to continue at rates comparable to those of the recent past. Owners' returns from capital appreciation have outpaced income realized from farm operations in every year since 1971.

To be effective, any law narrowing the definition of who may receive payments would necessarily have to exclude tenants of ineligible entities. Otherwise, leasing arrangements could easily be employed whereby the payments would, in essence, go to corporations or partnerships in the form of rents. However, excluding tenants from payments would mean that 9,000 or more family farms would be unable to participate in commodity programs.

Large-scale investors in farming are currently subject to a payments ceiling of $40,000 for feed grains, wheat, and cotton, and $52,250 for rice. A prohibition would, in effect, reduce the payments ceiling to zero for the affected entities. The existing payment ceiling has not had a significant impact on the farm sector. It has affected only a limited number of producers, many of whom were able to circumvent the legislation. To attempt to restrict the farming activities of outside investors by prohibiting payments to ineligible producers could prove as elusive an objective as have the goals of earlier measures limiting payments.

If legislation governing a payment prohibition were tightly written and subject to little circumvention, the impact of the prohibition would still vary among commodities. The profitability to excluded entities of producing wheat, sorghum, barley, and rice would likely diminish since programs for those crops have provided a substantial level of deficiency payments. There would be little impact on the incomes of producers of corn as payments for this crop has been relatively minor in recent years. A prohibition might, as a result, be expected to provide an incentive for ineligible firms to shift to specializing in crops for which payments have not been important or have not been available such as corn or soybeans. Excluded entities might also increase their production of other nonprogram commodities, including fruits, vegetables, livestock, and dairy, but most producers would be unable to shift quickly to nonpayment crops. The opportunities for major shifts between crops is limited by specialization and adaptation of crops.

The most immediate impact of a prohibition would be to end the participation by excluded groups in the set-aside and diversion programs. No longer constrained to reduce acreages under cultivation to remain eligible for payments, many of those excluded would place a greater proportion of their holdings in production.

Payment prohibitions affect progressively more units primarily engaged in farming as they are more broadly applied. In this sense they have more unintended impacts. For example applying a payment prohibition to ineligible corporations and their tenants (Option IV) affects 17 thousand units, over half of which are tenants, usually thought of as family farmers. Applying the payment prohibition most broadly (Option VI) affects over 38 thousand units, of which over 30 thousand are tenants or partnerships among related individuals. These, too, have traditionally been encouraged as family farms. The impacts on these tenants and partnerships would be to discourage entry into farming through either of these routes.

In summary, a payment prohibition could have a modest impact. A significant change in the degree of nonfarmer investment in agriculture would not be expected; however, the overall involvement in agriculture of those not primarily engaged in farming could be reduced slightly with some additional shift to the production of nonpayment commodities over time. Two potential routes to entry into farming would be discouraged--entry by tenancy and entry by partnership with a nonfarm investor. The legislative and administrative controls needed to make payment prohibitions effective would have to be carefully considered and could be costly; otherwise, producers would be able to avoid them as they generally have avoided payment ceilings in the past.

Appendix

CONGRESSIONAL MANDATE FOR THE PAYMENT PROHIBITION STUDY

Exhibit 1--Public Law 95-113, September 29, 1977

Study on Prohibiting Payments to Certain Legal Entities

Sec. 103. In furtherance of the policy stated in section 102 of this Act, the Secretary of Agriculture shall conduct a study and report to Congress no later than January 1, 1979, on the impact on participation in the wheat, feed grain, cotton, and rice programs and the production of such commodities in carrying out a statutory provision such as that included in the Food and Agriculture Act of 1977, as passed by the Senate on May 24, 1977, prohibiting the making of payments to certain corporations and other entities under such programs. The study shall, in addition, assess the impact of extending the prohibition against making commodity program payments to tenants on land owned by such corporations and other entities which would be excluded from payments under such a provision. The study shall utilize to the greatest extent possible, the information on commodity program payments compiled by the Agricultural Stabilization and Conservation Service in determining payment eligibility under section 101 of the Agricultural Act of 1970, as amended, and section 101 of this Act. The Secretary may collect such other information as may be necessary to determine the impact of such a statutory provision and to identify the number and characteristics of producers that would be affected by such a provision.

Exhibit 2--Section 101, subsection (b) of S. 275 of the Senate of the United States May 24, 1977

"(b) No payment otherwise payable under the annual programs established under the Agricultural Adjustment Act of 1938, as amended, and the Agricultural Act of 1949, as amended, for the 1978 through 1982 crops of wheat, feed grains, upland cotton, extra long staple cotton, and rice may be made to any person except--

"(1) a sole proprietorship farming operation (including any individual operating a farm as a tenant);

"(2) a corporation or other entity engaged in a farming operation if a controlling interest in such corporation or other entity is held by individuals engaged primarily in farming;

"(3) a small business corporation as defined in section 1371(a) of the Internal Revenue Code of 1954;

"(4) a trust or similar arrangement which involves the production of wheat, feed grains, cotton, or rice, and which was established on or after the date of enactment of the Food and Agriculture Act of 1977 by one or more persons who would have been eligible for payments under this subsection had such persons been engaged in a farming operation themselves on the land with which such trust or similar arrangement is concerned;

"(5) a trust or similar arrangement which involves the production of wheat, feed grains, cotton, or rice, and which was established by any person prior to the date of enactment of the Food and Agriculture Act of 1977;

"(6) an organization described in section 501(c)(3) of the Internal Revenue Code of 1954 and which is exempt from taxation under section 501(a) of such Code;

"(7) a partnership or similar arrangement in which each partner or owner would, if engaged in a farming operation on his own, be eligible for payments under this subsection; and

"(8) any State, political subdivision, or agency thereof".